

State Capitalism and the Foreign Corrupt Practices Act

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Who is a “foreign official” under the Foreign Corrupt Practices Act (FCPA)? This question will take on increasing importance in the coming years for two reasons. First, the Department of Justice (DOJ) and the Securities and Exchange Commission (SEC) are aggressively pursuing FCPA cases and, as a consequence, testing the boundaries of the statute. Second, many foreign governments appear to be returning to the old-time religion of state capitalism. Foreign governments act as state capitalists not just through state-owned enterprises, but also through public pension funds and sovereign wealth funds (SWFs); these funds are perhaps the next frontier for FCPA enforcement. Indeed, in 2011 the SEC put certain banks and private equity funds on notice that the agency’s enforcement staff had begun to take a closer look at the banks’ and funds’ dealings with SWFs. This Article examines SWFs and other state-controlled funds, including public pension funds, as “instrumentalities” and their employees as “foreign officials” under the FCPA. The Article concludes that although in some cases SWF and state-pension-fund employees would be “foreign officials” for purposes of the FCPA, in most cases the FCPA should not apply to these funds and their employees because there is no link between the employees and the type of foreign policy concern that motivated the creation of the FCPA.

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I. INTRODUCTION

From 2003 to 2005, Brian Travis and Nicholas Vulpis, employees of investment adviser JLF Asset Management, were alleged to have solicited and accepted bribes from David Baker, Daniel Schreiber, and Granite Financial Group, LLC, brokers who sought to retain business from JLF.¹ According to the SEC, Travis and Vulpis received “international air travel (including for family members), hotel arrangements, the cost of building a special crate to transport Travis’ Great Dane, fully-paid vacations, daily car service, computer equipment, and monthly rent payments for a personal residence. Collectively,

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¹ *Litigation Release No. 20948*, U.S. SEC. & EXCHANGE COMMISSION (Mar. 12, 2009), <http://www.sec.gov/litigation/litreleases/2009/lr20948.htm>.

Travis and Vulpis received at least \$312,000 in such personal benefits.”² In exchange for these services, Vulpis and Travis directed trades to Granite through Baker and Schreiber, and over the same period, Granite, Baker, and Schreiber received trading commissions of \$10,702,105.³ The SEC highlighted the material conflict of interest created by the bribery and noted that Travis and Vulpis attempted to conceal the amount of trades directed through Granite, as well as the amount of commissions paid to Granite.⁴

The SEC charged all of the parties with violations of antifraud statutes under the Securities Act of 1933 and the Securities Exchange Act of 1934, and aiding and abetting JLF’s violation of similar antifraud statutes under the Investment Advisers Act of 1940.⁵

All of the parties—the bribers and the bribed—settled with the SEC.⁶ In each case, the parties accepted the standard injunction against future violations of the antifraud statutes they were alleged to have violated.⁷ In addition, the bribers Baker, Schreiber, and Granite were fined, respectively, \$100,000, \$100,000, and \$250,000.⁸ Travis, one of the bribed hedge-fund employees, was required to disgorge \$107,965, pay an equal amount as a penalty, and also pay prejudgment interest of \$35,029.⁹ Vulpis, the other bribed employee, was required to disgorge \$105,450, pay a penalty of \$100,000, and pay prejudgment interest of \$32,381.¹⁰

The Granite/JLF case involved the sort of act that falls within the reach of the FCPA. The FCPA prohibits, in the words of DOJ, the

willful use of the mails or any means of instrumentality of interstate commerce corruptly in furtherance of any offer, payment, promise to pay, or authorization of the payment of money or anything of value to any person, while knowing that all or a portion of such money or thing of value will be offered, given or

² *Id.*

³ *Id.*

⁴ *Id.*

⁵ *Id.*; see also Securities Act of 1933 § 17(a), 15 U.S.C. § 77q(a) (2006); Securities Exchange Act of 1934 § 10(b), 15 U.S.C. § 78j(b) (2006); Investment Advisers Act of 1940 § 206(1)–(2), 15 U.S.C. § 80b-6(1)–(2) (2006). The SEC also charged the parties with a violation of the SEC rule relating to § 10(b), Rule 10b-5, 17 C.F.R. § 240.10b-5 (2008).

⁶ *Litigation Release No. 21390*, U.S. SEC. & EXCHANGE COMMISSION (Jan. 22, 2010), www.sec.gov/litigation/litreleases/2010/lr21390.htm; *Litigation Release No. 21466*, U.S. SEC. & EXCHANGE COMMISSION (Mar. 29, 2010), www.sec.gov/litigation/litreleases/2010/lr21466.htm.

⁷ *Litigation Release No. 21390*, U.S. SEC. & EXCHANGE COMMISSION (Jan. 22, 2010), www.sec.gov/litigation/litreleases/2010/lr21390.htm; *Litigation Release No. 21466*, U.S. SEC. & EXCHANGE COMMISSION (Mar. 29, 2010), www.sec.gov/litigation/litreleases/2010/lr21466.htm.

⁸ *Litigation Release No. 21390*, U.S. SEC. & EXCHANGE COMMISSION (Jan. 22, 2010), www.sec.gov/litigation/litreleases/2010/lr21390.htm.

⁹ *Litigation Release No. 21466*, U.S. SEC. & EXCHANGE COMMISSION (Mar. 29, 2010), www.sec.gov/litigation/litreleases/2010/lr21466.htm.

¹⁰ *Id.*

promised, directly or indirectly, to a foreign official to influence the foreign official in his or her official capacity, induce the foreign official to do or omit to do an act in violation of his or her lawful duty, or to secure any improper advantage in order to assist in obtaining or retaining business for or with, or directing business to, any person.¹¹

The only element missing in this case, of course, is the presence of a foreign official. But suppose that JLF was a sovereign wealth fund or a national pension fund: even though Travis and Vulpis might be compensated like private-fund managers, and even if they do not consider themselves to be foreign officials (in fact, they may not even be nationals of the state for whom the fund is managed), under FCPA interpretations used by DOJ and the SEC, Travis and Vulpis would very likely be deemed “foreign officials,” and so Baker, Schreiber, and Granite would be facing civil FCPA charges as well as criminal FCPA charges, in addition to the charges that would normally accompany such allegations.

The application of the FCPA to state-controlled enterprises and foreign funds raises a host of issues that are only just beginning to be addressed in the growing literature on the FCPA.¹² This short Article, written as part of the *Ohio State Law Journal*’s symposium on the FCPA, attempts to sketch out some of these issues.

First, it is unclear whether the FCPA can or should be read to cover foreign funds. There are several practical reasons for arguing that it should not, among them a recognition that most of these enterprises and funds operate as quasi-independent entities that should not be viewed as direct agents of their respective governments. These funds, especially, also typically serve economic and financial purposes, rather than a political or governmental purpose.

Second, even if foreign enterprises and funds can be viewed as foreign instrumentalities, it is not clear that the FCPA provides the best remedy for the type of harm that the JLF/Granite case highlights. The SEC characterized the harm committed by the JLF employees, Travis and Vulpis, as a breach of fiduciary duty to the hedge-fund investors; the Granite employees, Baker and Schreiber, facilitated this breach through their bribes. Cast in these terms, the harm was an agency cost, and the SEC assisted the hedge-fund investors by applying their enforcement resources to cover some of the costs of monitoring the agents of the investors, Travis and Vulpis. If the hedge-fund investors are the beneficiaries of this shifting of agency costs from private investors to public enforcers, who are the beneficiaries of a similar shift when Baker and Schreiber are viewed to have bribed foreign officials?

A third concern, related to the foregoing, is the apparent agency and judicial drift away from the original purpose of the FCPA as a tool to prevent corruption

¹¹ *Foreign Corrupt Practices Act: An Overview*, U.S. DEP’T OF JUSTICE, <http://www.justice.gov/criminal/fraud/fcpa/> (last visited Aug. 24, 2012).

¹² See, e.g., Court E. Golumbic & Jonathan P. Adams, *The “Dominant Influence” Test: The FCPA’s “Instrumentality” and “Foreign Official” Requirements and the Investment Activity of Sovereign Wealth Funds*, 39 AM. J. CRIM. L. 1 (2011).

that affects foreign policy. If this original purpose is to have any meaning in the context of state-controlled enterprises and funds, there must be a link between the foreign government, the instrumentality of the government, and the foreign officials who work for the instrumentality. Each of these entities must be connected like three links of a chain—the foreign government linked to the instrumentality, and the instrumentality linked to the foreign official. In this way, the acts of the foreign government have an effect on the foreign official, and the acts of the foreign official have an effect on the government. Only if there exists this linkage between the foreign official and the foreign government—in the case of state-controlled enterprises and state-controlled funds, through their respective links to an instrumentality—should we expect to find the kind of foreign-policy effect that the FCPA was designed to police. Current SEC and DOJ interpretations, as well as the scant jurisprudence that has tested these interpretations, tend to look only at the connection between the foreign government and the instrumentality. The legislative history of the FCPA, however, suggests that because foreign-policy concerns are central to the FCPA, the link between the instrumentality and the foreign official must also be tested.

This Article attempts to get at the core issue of the proper scope of the FCPA by considering who is an “instrumentality” and “foreign official” under the statute. Additional clarity could be brought to this question by looking first at the link between the foreign government and alleged instrumentality. Other areas of the law, including foreign investment law, have developed a substantial base of knowledge on the issues of foreign government control of state-affiliated enterprises and funds that could help inform FCPA jurisprudence. As noted above, however, the more significant problem concerns the unidirectionality of current tests for “instrumentality” and “foreign official” status. The tests used by the few courts addressing the issue have tended to look only at the issue of governmental control, but have ignored the link between the foreign official and the instrumentality—in other words, does the foreign official exercise control over the instrumentality so that there is a meaningful connection between the foreign government and the foreign official? This analysis is key because if one takes the legislative history of the FCPA seriously, an FCPA prosecution is predicated on the ability of the foreign official to affect foreign policy.

In Part II, I examine the FCPA’s “foreign official” definition as applied to sovereign wealth funds and other governmental funds like state pension funds. The expansion of this definition is increasingly important as these funds play an increasingly larger role in our capital markets. This is particularly true of Chinese funds.

In Part III, I examine the criminalization of agency costs implicit in an FCPA action involving bribery of an official or agent of a foreign fund. I will also consider the problematic application of the FCPA to foreign instrumentalities as investors—consider, for example, whether a private equity fund could be considered the instrumentality of a foreign government if it

manages a fund in which a sovereign wealth fund or a state-owned pension fund is one of many investors. Part IV concludes.

II. THE FCPA'S "FOREIGN OFFICIAL" DEFINITION

The FCPA has two main components. First, the FCPA put in the Securities Exchange Act of 1934 (Exchange Act) a series of books-and-records provisions that in essence require companies to maintain internal controls systems and disclosure systems to make it harder to conceal (and attach penalties to the concealment of) "slush funds" within a firm's financial statements.¹³ Second, the FCPA enacted anti-bribery provisions that prohibit both "domestic concerns," such as U.S. citizens and U.S. businesses and their personnel, as well as foreign persons in U.S. territory and foreign companies that have shares listed on a U.S. stock exchange, or are otherwise reporting companies under the Exchange Act, from corruptly paying, offering to pay, or authorizing payment

of anything of value to any foreign official for purposes of influencing any act or decision of such foreign official in his official capacity, inducing such foreign official to do or omit to do any act in violation of the lawful duty of such official, or securing any improper advantage . . . in order to . . . obtain[] or retain[] business.¹⁴

Unpacking all the definitions in the FCPA is a daunting task, not least because DOJ and the SEC have added to the baggage through expansive definitions of key terms, many of which are not challenged in court for reasons amply explained by other scholars.¹⁵ The key term that is most central to this Article's discussion is "foreign official." "Foreign official" is defined by the statute as:

[A]ny officer or employee of a foreign government or any department, agency, or instrumentality thereof, or of a public international organization, or any person acting in an official capacity for or on behalf of any such government or department, agency, or instrumentality, or for or on behalf of any such public international organization.¹⁶

Key components of that definition—particularly "instrumentality"—are left undefined by the statute. The *Carson* case involved payments by former officers of Control Components Inc. to executives or other employees of state-owned

¹³ See 15 U.S.C. § 78m(b) (2006).

¹⁴ *Id.* § 78dd-2(a).

¹⁵ See, e.g., Mike Kohler, *The Façade of FCPA Enforcement*, 41 GEO. J. INT'L L. 907, 917–18 (2010); Joseph W. Yockey, *Solicitation, Extortion, and the FCPA*, 87 NOTRE DAME L. REV. 781, 812–25 (2011).

¹⁶ 15 U.S.C. § 78dd-1(f)(1)(A) (2006).

enterprises.¹⁷ The government argued that the state-owned enterprises were “instrumentalities” within the meaning of the FCPA.¹⁸ In Professor Michael Koehler’s exhaustive review of the legislative history, prepared as expert testimony in *United States v. Carson*, Professor Koehler stressed:

[T]here is no express statement or information in the FCPA’s legislative history to support the DOJ’s expansive legal interpretation that alleged SOEs are “instrumentalities” (or “departments” or “agencies”) of a foreign government and that employees of SOEs are therefore “foreign officials” under the FCPA’s anti-bribery provisions.

However, there are several statements, events, and information in the FCPA’s legislative history that demonstrate that Congress did not intend the “foreign official” definition to include employees of SOEs.¹⁹

Koehler also noted that foreign-policy concerns primarily animated the FCPA’s enactment;²⁰ the implication of this observation is that a state-owned enterprise is often likely to have at best only a tenuous connection to foreign policy concerns.

By Koehler’s count, the SEC and DOJ’s untested, expansive definition of foreign official in the context of state-controlled enterprises was at the core of six out of nine FCPA cases brought in 2009,²¹ twelve out of twenty cases in 2010,²² and thirteen of sixteen cases in 2011.²³ While it is clear that a foreign finance minister would be considered a foreign official for purposes of the FCPA, what about lower-ranking officials? And what if these officials serve not as ministry employees, but as employees of a state-managed pension fund or a sovereign wealth fund? In such cases, the DOJ and SEC appear to view these funds as instrumentalities²⁴ of the government, and so each of their employees

¹⁷ *United States v. Carson*, No. SACR 09-00077-JVS, 2011 WL 5101701, at *1 (C.D. Cal. May 18, 2011).

¹⁸ *Id.* at *3.

¹⁹ Declaration of Professor Michael J. Koehler in Support of Defendants’ Motion to Dismiss Counts One Through Ten of the Indictment at 4, *United States v. Carson*, No. SA CR 09-00077-JVS, 2011 WL 5101701 (C.D. Cal. May 18, 2011).

²⁰ *Id.* at 5.

²¹ Koehler, *supra* note 19, at 966.

²² Mike Koehler, *The Akim of Nookat, Lots of Nigerian Customs Officials, the Congo Merchant Marine, and Lots of Telecom Employees—The “Foreign Officials” of 2010*, FCPA PROFESSOR (Jan. 24, 2011), <http://www.fcpaprofessor.com/the-akim-of-nookat-lots-of-nigerian-customs-officials-the-congo-merchant-marine-and-lots-of-telecom-employees-the-foreign-officials-of-2010>.

²³ Mike Koehler, *Healthcare Providers, Telecom (and Other SOE) Employees, Veterinarians, and Liquor Store Employees—The “Foreign Officials” of 2011*, FCPA PROFESSOR (Jan. 17, 2012), <http://www.fcpaprofessor.com/healthcare-providers-telecom-and-other-soe-employees-veterinarians-and-liquor-store-employees-the-foreign-officials-of-2011>.

²⁴ See Dionne Searcey & Randall Smith, *SEC Probes Banks, Buyout Shops over Dealings with Sovereign Funds*, WALL ST. J. (Jan. 14, 2011), <http://online.wsj.com/article/>

would be a foreign official under the FCPA.²⁵ This follows from interpretative guidance by DOJ that, although not directly on point, makes clear that foreign funds would fall within the agencies' definition of an instrumentality.

Most of this guidance, like much of the case law that has challenged it, considers whether an employee of a state-owned enterprise should be considered a "foreign official." In a 1994 FCPA Opinion Procedure Release, DOJ stated that it would treat as a foreign official an employee of a state-owned enterprise even though the domestic concern dealing with the state-owned enterprise had been advised that under the nation's law, "the [employee] would not be regarded as either a government employee or a public official."²⁶ This understanding was echoed in public comments by Peter Clark, Deputy Chief of DOJ's Fraud Section, Criminal Division, who supervised FCPA enforcement. Clark counseled that companies attempting to determine whether a "government-owned commercial enterprise" was a foreign official under the FCPA should focus on issues of control and influence.²⁷ Thus, not only is the government's percentage of ownership or voting rights important in making the determination, but also whether the entity's employees "hold governmental roles, have the rights and privileges of government positions, or are capable of exerting influence on the government."²⁸

In one (and perhaps the only) instance, DOJ has indicated that the foreign government's own estimation of whether a state-owned enterprise is an instrumentality of the foreign government may be significant. In comments

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²⁵ In a recent *Business Lawyer* article, attorneys Joel M. Cohen, Michael P. Holland, and Adam P. Wolf collect a sample of cases in which state-owned enterprises have been classified as "instrumentalities," including: the Baker Hughes Information case in which, according to DOJ, "Kazakhoil was controlled by officials of the Government of Kazakhstan" and thereby was an "instrumentality" of the Kazakhstan government, making its employees foreign officials under the FCPA; the DPC (Tianjin) Co. Ltd. case, in which DPC was charged with FCPA violations for "making payments totaling approximately \$1.6 million to physicians and laboratory personnel employed by government-owned hospitals in China to influence their decisions to purchase the company's products"; and also in the Alcatel case, in which DOJ alleged that Alcatel made "corrupt payments . . . to officials of Instituto Costarricense de Electricidad, Costa Rica's state-owned telecommunications authority." Joel M. Cohen et al., *Under the FCPA, Who Is a Foreign Official Anyway?*, 63 BUS. LAW. 1243, 1250 n.26 (2008).

²⁶ Foreign Corrupt Practices Act Review, Op. Proc. Release No. 94-01 (Dep't of Justice May 13, 1994), available at <http://www.usdoj.gov/criminal/fraud/fcpa/opinion/1994/9401.pdf>. Because the parties agreed to contractually mitigate the risk that the employee would not influence government policy, DOJ determined that it would not pursue enforcement against the domestic concern. See *id.*

²⁷ Cohen et al., *supra* note 25, at 1254 (citing Peter B. Clark, Deputy Chief, Fraud Section, Criminal Div., U.S. Dep't of Justice, Statement Before the American Bar Association Conference on the Foreign Corrupt Practices Act (Feb. 21, 1997)).

²⁸ *Id.*

provided to the Organization for Economic Co-operation and Development (OECD) Working Group on Bribery, DOJ stated that:

[S]tate-owned business enterprises may, *in appropriate circumstances*, be considered instrumentalities of a foreign government and their officers and employees to be foreign officials. Among the factors that [DOJ] considers are the foreign state's own characterisation of the enterprise and its employees, i.e., whether it prohibits and prosecutes bribery of the enterprise's employees as public corruption, the purpose of the enterprise, and the degree of control exercised over the enterprise by the foreign government.²⁹

In their review of the foreign-official definition, attorneys Joel Cohen, Michael Holland, and Adam Wolf argue that domestic firms would prefer a definition based on the foreign government's own characterization to the more malleable categorization of instrumentality through evidence of control or influence:

This consideration might be helpful to companies subject to the FCPA because they can reasonably inquire during the course of due diligence of a potential or current customer how that customer's local regulators classify it (i.e., do they view the customer as a public or private enterprise?). Unlike the arbitrary determination of how much "control" a foreign government exercises over a particular company, in many cases there will be a definite answer to this question, as a company should be able to determine how it is characterized by its local government. Moreover, a domestic regulator is better able to identify its own "officials" or "instrumentalities" than the DOJ, SEC, or an entity subject to the FCPA.³⁰

It is prudent for domestic firms to read DOJ's OECD comments as inclusive, not exclusive; a state-owned enterprise that might not satisfy the control or influence standard could nonetheless be categorized as an instrumentality, and its employees as public officials, if the foreign government considers the business and its employees as such. DOJ or SEC is unlikely to exclude a state-owned enterprise from the definition of instrumentality even if the foreign government has not so categorized it. As Cohen, Holland, and Wolf note, "[o]f course, the DOJ and SEC are not bound to adhere to the views of the foreign government regarding whether one of its companies is an 'instrumentality' of that government, especially if the DOJ or SEC suspects that the government is itself corrupt."³¹

In more recent comments, DOJ has stressed the control and influence factors as the primary triggers for instrumentality status. Mark Mendelsohn,

²⁹ *United States: Review of Implementation of the Convention and 1997 Recommendation*, ORG. FOR ECON. CO-OPERATION & DEV. 1, 6 (Apr. 1999), <http://www.oecd.org/dataoecd/16/50/2390377.pdf>.

³⁰ Cohen et al., *supra* note 25, at 1254-55.

³¹ *Id.* at 1255 n.50.

recently the Deputy Chief of DOJ's Fraud Section and supervisor over FCPA enforcement, stated in 2008 that DOJ considers "all employees of public entities" to be "public officials,"³² and agreed with the assertion that for a foreign firm to be considered an instrumentality, "certainly over fifty percent [government ownership] is [sufficient], and I think there are certainly instances under fifty percent where it may well be."³³ In 2009, Lanny Breuer, Assistant Attorney General, gave a sense of the breadth of the government's view of "instrumentality" and "foreign official" definitions when he opined to a conference of pharmaceutical compliance professionals that:

Some [persons that would fall within the definition of "foreign official"] are obvious, like health ministry and customs officials of other countries. But some others may not be, such as the doctors, pharmacists, lab technicians and other health professionals who are employed by state-owned facilities. Indeed, it is entirely possible, under certain circumstances and in certain countries, that nearly every aspect of the approval, manufacture, import, export, pricing, sale and marketing of a drug product in a foreign country will involve a "foreign official" within the meaning of the FCPA.³⁴

The lack of certainty surrounding a control- or influence-based definition is undoubtedly frustrating to practitioners and, more importantly, the companies that they represent. Somewhat more certainty is found in many other areas of law dealing with foreign entities, in part because these other areas have definitional sections and interpretive materials that help guide firms' conduct. Although Cohen, Holland, and Wolf note that the government deviates from strict control- and influence-based standards in the Foreign Sovereign Immunities Act³⁵ and statutes dealing with criminal acts against foreign

³²*Id.* at 1255; *see also* JOSEPH P. COVINGTON ET AL., JENNER & BLOCK, FCPA ENFORCEMENT TRENDS 1 (Oct. 24, 2007), *available at* <http://www.jenner.com/system/assets/publications/1069/original/FCPAEnforcementTrends.pdf?1314127199> ("For example, Mendelsohn explained, DOJ construes the term 'Public Official' to include the employees of public entities.").

³³Cohen et al., *supra* note 25, at 1255.

³⁴Lanny A. Breuer, Assistant Attorney Gen., U.S. Dep't of Justice, Prepared Keynote Address to the Tenth Annual Pharmaceutical Regulatory and Compliance Congress and Best Practices Forum (Nov. 12, 2009), *available at* www.ehcca.com/presentations/pharmacongress10/breuer_2.pdf.

³⁵They note that under the FSIA, a "foreign state 'includes a political subdivision of a foreign state or [an] agency or instrumentality of a foreign state'" and that "[a]n 'agency or instrumentality' is defined as any entity that is (1) a separate legal person; (2) an organ or political subdivision of the foreign state, or owned by the foreign state; and (3) neither a U.S. citizen nor created under the laws of a third country." Cohen et al., *supra* note 25, at 1258 (quoting Foreign Sovereign Immunities Act of 1976 §§ 2(a)–4(a), 28 U.S.C. § 1603(a)–(b) (2006)). Reviewing the legislative history, they further note that "[t]he House of Representatives considered a 'separate legal person' to include a corporation that could sue, contract, or hold property in its own name." *Id.* (citing H.R. REP. NO. 94-1487, at 15 (1976), *reprinted in* 1976 U.S.C.C.A.N. 6604, 6613–14). A corporation "would be considered an

officials, other areas of the law, particularly those dealing with foreign investment, utilize control and influence standards within the applicable statutes and interpretive guidance.

An example of this is the Exon-Florio legislation, as recently amended by the Foreign Investment and National Security Act of 2007 (FINSA).³⁶ Under Exon-Florio, controlling investments by foreign entities, including SWFs, that implicate national security issues are regulated through a voluntary filing and review process coordinated through CFIUS. The CFIUS process governs “any merger, acquisition, or takeover that is proposed . . . by or with any foreign person which could result in foreign control of any person engaged in interstate commerce in the United States,”³⁷ and focuses on investments that may have a security impact on “critical infrastructure.”³⁸ Under recently enacted regulations from the Treasury Department, control is:

the power, direct or indirect, whether or not exercised, through the ownership of a majority or a dominant minority of the total outstanding voting interest in an entity, board representation, proxy voting, a special share, contractual arrangements, formal or informal arrangements to act in concert, or other means, to determine, direct, or decide important matters affecting an entity.³⁹

The regulations then list decisions that demonstrate control, such as the sale or encumbrance of assets, reorganizations or merger of the equity or debt, selection of business ventures, entering into or terminating significant contracts, altering policies for control of sensitive information, appointment or dismissal of senior officers, appointing or dismissing persons with access to sensitive information, and amending organizational documents.⁴⁰

Under the CFIUS process, parties to a covered transaction typically file a voluntary notice, often even when it appears that the transaction does not involve a controlling ownership. After notice is received, CFIUS undertakes a thirty-day “National Security Review.”⁴¹ Following this review, CFIUS may either allow the transaction to proceed, or may undertake a second, forty-five-

‘agency or instrumentality’ of its government only if a *majority* of its ownership interests were owned by the foreign state or a political subdivision of that state.” *Id.* (emphasis added). They note that “companies that were merely ‘government-controlled’ were not mentioned as falling within the FSIA’s definition of ‘agency or instrumentality.’” *Id.*

³⁶ This Article’s discussion of the application of Exon-Florio is based on (and amplified in) Paul Rose, *Sovereign Wealth Fund Investment in the Shadow of Regulation and Politics*, 40 GEO. J. INT’L L. 1207 (2009); see also Foreign Investment and National Security Act of 2007, Pub. L. No. 110-49, 121 Stat. 246 (codified at 50 U.S.C.A. app. § 2170 (West 2012)).

³⁷ 50 U.S.C. app. § 2170(a)(3) (2006).

³⁸ *Id.* § (6).

³⁹ Regulations Pertaining to Mergers, Acquisitions, and Takeovers by Foreign Persons, 31 C.F.R. § 800.204 (2008).

⁴⁰ *Id.* § 800.204(a)(1)–(10).

⁴¹ 50 U.S.C. app. § 2170(b)(1) (2006).

day “National Security Investigation.”⁴² Certain transactions, however, automatically require the second-stage review,⁴³ including foreign government-controlled transactions, which are defined as transactions in which an entity controlled by or acting on behalf of a foreign government seeks to engage in “any merger, acquisition, or takeover” which “could result in the control of any person engaged in interstate commerce in the United States” that could affect the national security of the United States.⁴⁴ An exception to this requirement is a finding by senior CFIUS officials that, after review, the transaction will not impair the national security of the United States. The Treasury has also put in place regulations under which transactions resulting in a foreign person holding ten percent or less of a U.S. interest will not be considered “covered transactions,” provided the acquisition is passive and does not bring with it the incidents of control for the foreign investor, such as a seat on the board of directors.⁴⁵

A number of industry-specific regulations also focus on control- and influence-based standards in determining whether or not heightened regulation is necessary. An example of this is the banking sector and the provisions governing investment in the Bank Holding Company Act (BHCA)⁴⁶ and the Change in Bank Control Act of 1978.⁴⁷ The BHCA requires an investor to obtain approval from the Federal Reserve before acquiring a direct or indirect interest in a U.S. bank or bank holding company if the investment exceeds certain control thresholds. These thresholds include investments in which:

the company directly or indirectly or acting through one or more other persons owns, controls, or has power to vote 25 per centum or more of any class of voting securities of the bank or company; the company controls in any manner the election of a majority of the directors or trustees of the bank or company; or the [Federal Reserve] determines, after notice and opportunity for hearing, that the company directly or indirectly exercises a controlling influence over the management or policies of the bank or company.⁴⁸

The third category of investment—situations in which the investor may exercise a “controlling influence”—presents a concern similar to that faced by companies dealing with the FCPA. Looking to either the BHCA or Exon-Florio for guidance may be of little comfort, however, since the striking feature of these regulations is the relatively low threshold for influence in terms of ownership percentage. Speaking before the Senate Banking Committee on

⁴² *Id.* § 2170(b)(2).

⁴³ *Id.*

⁴⁴ 50 U.S.C. app. § 2170(a)(3)–(4) (2006). *Id.* § 2170(b)(2).

⁴⁵ Regulations Pertaining to Mergers, Acquisitions, and Takeovers by Foreign Persons, 31 C.F.R. § 800.302(b) (2008).

⁴⁶ Bank Holding Company Act of 1956, 12 U.S.C. § 1841 (2006).

⁴⁷ Change in Bank Control Act of 1978, 12 U.S.C. § 1817(j) (2006).

⁴⁸ 12 U.S.C. § 1841(a)(2)(A)–(C) (2006).

sovereign-wealth-fund investment in U.S. financial institutions, Federal Reserve Board General Counsel Scott Alvarez stated that:

In determining whether an investor may exercise a controlling influence over the management or policies of a U.S. banking organization and thereby trigger formal review of the investment, the Board considers the size of the investment, the involvement of the investor in the management of the banking organization, any business relationships between the investor and the banking organization, and a number of other relevant factors.

The Bank Holding Company Act itself presumes that an investor that controls less than 5 percent of the voting shares of a banking organization does not have a controlling influence over that organization, and based on its experience, the Board generally has not found that a controlling influence exists if the investment represents less than 10 percent of the organization's voting shares.⁴⁹

As we review the case law that has resulted from challenges to the SEC and DOJ's broad interpretation of "instrumentality" and "foreign official," it becomes clear that a similar control/influence standard has begun to take hold in some U.S. district courts. In *United States v. Aguilar*,⁵⁰ a 2011 California District Court case involving the alleged bribery of officials of the Mexican Comisión Federal de Electricidad,⁵¹ the court held that an "instrumentality" may include government-controlled agencies or businesses in which:

- The entity provides a service to the citizens—indeed, in many cases to all the inhabitants—of the jurisdiction.
- The key officers and directors of the entity are, or are appointed by, government officials.
- The entity is financed, at least in large measure, through governmental appropriations or through revenues obtained as a result of government-mandated taxes, licenses, fees or royalties, such as entrance fees to a national park.
- The entity is vested with and exercises exclusive or controlling power to administer its designated functions.
- The entity is widely perceived and understood to be performing official (i.e., governmental) functions.⁵²

⁴⁹ *Foreign Government Investment in the U.S. Economy and Financial Sector: Joint Hearing Before the Subcomm. on Domestic and Int'l Monetary Policy, Trade, and Tech. and the Subcomm. on Capital Markets, Ins., and Gov't Sponsored Enterprises of the H. Comm. on Fin. Services*, 110th Cong. 13 (2008) (statement of Scott G. Alvarez, General Counsel, Board of Governors of the Federal Reserve System).

⁵⁰ *United States v. Aguilar*, 783 F. Supp. 2d 1108 (C.D. Cal. 2011).

⁵¹ *Id.* at 1109.

⁵² *Id.* at 1115.

In the aforementioned 2011 *Carson* case, also decided by a California Central District Court, the test for an “instrumentality” was similarly defined by looking to:

- The foreign state’s characterization of the entity and its employees;
- The foreign state’s degree of control over the entity;
- The purpose of the entity’s activities;
- The entity’s obligations and privileges under the foreign state’s law, including whether the entity exercises exclusive or controlling power to administer its designated functions;
- The circumstances surrounding the entity’s creation; and
- The foreign state’s extent of ownership of the entity, including the level of financial support by the state (e.g., subsidies, special tax treatment, and loans).⁵³

Another test for whether a state-controlled enterprise is an instrumentality is found in the *Esquenazi* case,⁵⁴ in which the jury was instructed that the factors that may be considered in deciding whether a state-controlled enterprise is an instrumentality include:

- whether it provides services to the citizens and inhabitants of [the state];
- whether its key officers and directors are government officials or are appointed by government officials;
- the extent of [the government’s] ownership of [the enterprise], including whether the . . . government owns a majority of [the enterprise’s] shares or provides financial support such as subsidies, special tax treatment, loans, or revenue from government-mandated fees;
- [the enterprise’s] obligations and privileges under [the state’s] law, including whether [the enterprise] exercises exclusive or controlling power to administer its designated functions; and
- whether [the enterprise] is widely perceived and understood to be performing official or governmental functions.⁵⁵

The court noted that the factors are

not exclusive, and no single factor will determine whether [the enterprise] is an instrumentality of a foreign government. In addition, you do not need to find

⁵³ Order Denying Motion to Dismiss, *United States v. Carson*, No. 09-77 at 5 (C.D. Cal. May 18, 2011), 2011 WL 5101701, at *3–4. In both *Aguilar* and *Carson*, the court viewed these factors as a non-exclusive list. *Aguilar*, 783 F. Supp. 2d at 1115; *Carson*, 2011 WL 5101701, at *4. And in *Carson* the court also noted that “no single factor is dispositive.” *Carson*, 2011 WL 5101701, at *4.

⁵⁴ *United States v. Esquenazi*, 1:09-CR-21010, 2010 U.S. Dist. LEXIS 143572 (S.D. Fla. Aug. 5, 2011).

⁵⁵ Court’s Final Instructions to the Jury at 24, *United States v. Esquenazi*, 2010 U.S. Dist. LEXIS 143572 (S.D. Fla. Aug. 5, 2011) (No. 09-21010-CR-MARTINEZ).

that all the factors listed above weigh in favor of [the enterprise] being an instrumentality in order to find that [the enterprise] is an instrumentality.⁵⁶

The striking problem with the control/influence tests as applied to the FCPA is that they are top-down and unidirectional. The central focus of the tests is whether the foreign government can control the policies of the instrumentality. A top-down policy is clearly defensible in the context of investment regulations, since the concern is that the state-controlled business will serve as a political vehicle for the government owner. On the other hand, the concern that animated the passage of the FCPA was not the top-down use of instrumentalities, but rather the concern that an instrumentality could be used as a bottom-up means of influencing a foreign government's policies. Thus, if the legislative history is to have real meaning, instead of asking (or merely asking) whether the government has influence over the instrumentality, the question should be whether the person at the instrumentality who is receiving the bribe has the ability to influence government policies. That may be the case with the health-ministry official, for instance, but exceedingly unlikely to be the case with the hospital worker.

To align the tests used by the courts with the legislative intent of the FCPA, the question of whether an enterprise or fund is an instrumentality should be bi-directional: the core consideration for the courts should be whether the foreign official is somehow linked to governmental policy, such that a payment to the governmental official will somehow affect the foreign policy decisions of either the U.S. government or the foreign country. The definition of an instrumentality is key because it provides a link between the foreign country and the foreign official. If one is going to test the strength of the connection between the foreign official and the foreign country, the link between the foreign country and the instrumentality must be tested (and this is indeed the primary focus of the tests employed by the district courts), and the link between the foreign official and the instrumentality must also be tested. Only if both of these links are tested can one show full respect to the basic concern for foreign-policy effects that underlies the FCPA.

Making the FCPA test for foreign-official status bi-directional would not be difficult. As noted by Michael Volkov, an experienced FCPA litigator, a ready framework is already available:

... [W]hen it comes to state-owned-enterprises, when is it fair to treat such an enterprise as a "government entity?"

This fundamental question can be answered by considering the purposes of the FCPA, which was to prevent bribes or other improper payments which ultimately undermine the integrity of the foreign government and competition among businesses for government contracts or benefits. One does not need to look very far to answer this question—corporate law has already addressed these issues, and developed tools to evaluate whether or not a person, or group

⁵⁶ *Id.*

of people, exercise “control” over a company. That same inquiry can provide judges a firm foundation to build case law in the FCPA area.

The danger of bribes to government officials is that such acts skew decision-making contrary to the public interest. If the bribe recipient does not have control or sufficient influence within the enterprise to skew that process, then the government interest in the private company should not constitute an “instrumentality thereof.” Applying corporate principles of control to include factors such as ownership percentages, voting rights, participation in day-to-day management of the company, will provide the framework and the tools to develop adequate guidelines in this area.⁵⁷

To see the problems with a unidirectional approach to issues of control, consider the effects and the beneficiaries of enforcement of current tests which address one, but not both, of these links. If the test looks only to whether an instrumentality is linked to the government, it does not address the issue of whether a payment has any effect on foreign policy because it does not test whether the bribed foreign official has any impact on foreign policy considerations. It merely looks at whether an employee of the instrumentality is receiving a payment that, in keeping with his or her fiduciary responsibilities, he or she should not accept. To take one of the more egregious examples from 2011, do the purchasing decisions of a liquor-store employee of a state-owned liquor store affect foreign policy?⁵⁸ In this case it may have been perfectly sensible to conclude that the liquor stores were, in fact, state-owned enterprises, but this shows how such a top-down approach can produce ridiculous results without the limiting principle supplied by a bottom-up analysis of the impact of the alleged foreign official on the instrumentality and the government. Do their decisions impact foreign policy?

That Congress was in fact aware of the need for requiring a bottom-up analysis is seen in the “ministerial or clerical” employees exemption under the original definition of the “foreign official.” Although this exception was broken out as a stand-alone “facilitating payment” or “grease” exception,⁵⁹ Congress signaled that the original foreign policy justifications for the FCPA were undisturbed by the change:

The policy adopted by Congress in 1977 remains valid, in terms of both U.S. law enforcement and foreign relations considerations. Any prohibition under U.S. law against this type of petty corruption would be exceedingly difficult to enforce, not only by U.S. prosecutors but by company officials themselves. Thus while such payments should not be condoned, they may appropriately be excluded from the reach of the FCPA. U.S. enforcement

⁵⁷ Michael Volkov, *What Is an ‘Instrumentality Thereof’? Let’s Keep It Real*, FCPA BLOG (Mar. 9, 2011, 7:08 AM), <http://www.fcpablog.com/blog/2011/3/9/what-is-an-instrumentality-thereof-lets-keep-it-real.html>.

⁵⁸ In the Matter of Diageo plc, Exchange Act Release No. 64978, 2011 WL 3158087 (July 27, 2011).

⁵⁹ See Koehler, *supra* note 23.

resources should be devoted to activities having much greater impact on foreign policy.⁶⁰

When one strips away foreign-policy considerations from the test of whether a state fund or state-controlled enterprise employee is a foreign official, what is the result of the FCPA enforcement action? Or, to ask the question differently, who benefits from the enforcement action? The direct beneficiaries would be, in the case of state-controlled pension fund or sovereign wealth fund, the foreign government and, by extension, its citizens. The foreign government and its citizens receive whatever agency-cost savings that come from the payment of millions of dollars to monitor the fund's employees, paid not by the foreign government itself, but by U.S. taxpayers. In the case of state-controlled enterprises, the agency costs are again borne by the U.S. taxpayer, and the beneficiaries include not only the foreign government, but in many cases the majority of the benefits flow (at least indirectly) to the shareholders that own most of the stock in the enterprise. This perspective raises an important question in those cases in which foreign policy is not at issue: Why are U.S. taxpayers paying for enforcement that serves to reduce agency costs for foreign governments, their citizens, and in some cases, the stockholders of partially state-controlled enterprises, but has no effect on U.S. foreign policy considerations?

III. STATE-CONTROLLED FUNDS AS INSTRUMENTALITIES

If top-down tests such as those articulated in the *Carson*, *Aguilar*, and *Esquenazi* cases control questions of whether an employee is a foreign official, how would state-owned funds fit in this framework? Looking at these funds' function and the form that they typically take, one first notes that the funds generally mimic private entity forms, such as private pension funds or endowment funds. In the case of sovereign wealth funds and public pension funds, the actual management of the funds is not handled directly through a ministry of finance, but through a combination of specialist employees who are hired as in-house fund managers and external managers that receive mandates from the fund to invest a portion of the assets of the fund. In both of these cases, the managers hired by the fund may not be (and often are not) nationals of the sovereign state that owns the fund.

While the form of state-controlled funds is typically similar to privately controlled funds, the purposes of the fund naturally relate to state policies. Public pension funds serve a direct and relatively simple purpose: the provision of future benefits to employees and/or citizens of the state. Sovereign wealth funds are created for a variety of reasons.⁶¹ Some SWFs, for example, have

⁶⁰ H.R. REP. NO. 100-40, at 76–77 (1987).

⁶¹ Some of the discussion in this section is based on Paul Rose, *American Sovereign Wealth* (2012) (unpublished manuscript) (on file with author).

been created as a response to the so-called “Dutch Disease.” Dutch Disease refers to the phenomenon wherein resource exports lead to rising currency appreciation, which in turn affects the relative pricing of manufactured goods from the same country. As the currency appreciates, other products become less competitive, resulting in a distortion to the economy including a reduction in total exports. An SWF helps to protect against these effects by making use of currency reserves, thereby reducing the relative value of the currency in order to reduce negative effects on other exported products.

Sovereign wealth funds have also been explained as the policy instrumentalities of state capitalism. As argued by Gilson and Milhaupt:

[S]ome major developing countries (China foremost among them) increasingly reflect a form of state capitalism—what we call the new mercantilism. In this form, the country is the unit whose value is to be maximized, with a corresponding increase in the role of the national government as a direct participant in and coordinator of the effort.⁶²

As a general matter, it may be difficult to extricate the political from the economic when analyzing SWF creation and behavior. SWF and other state-owned enterprise investments occur against a backdrop of political relations between the SWF sponsor country and the target investment’s home country, and it should not be surprising that warm economics accompanies warm politics. For example, Jiang describes a significant reduction in Chinese investment in Canada from 2006 to 2009 as the newly elected conservative government attempted a “cold politics, warm economics” approach to China, with the result that “Canada lost ground in China on the economic and trade fronts.”⁶³ Ultimately, Canada’s government realized that the policy was hurting Canada much more than China, and “continued disengagement at the highest level would only put Canada in a more disadvantageous position.”⁶⁴ The investments themselves may also be made for hybrid political-economic purposes, of course: investments by Chinese enterprises and Chinese SWFs form part of the “go-out” strategy of the central government to seek out and secure reliable sources of energy and materials around the world in order to meet domestic manufacturing and energy demands.⁶⁵

⁶² Ronald J. Gilson & Curtis J. Milhaupt, *Sovereign Wealth Funds and Corporate Governance: A Minimalist Response to the New Mercantilism*, 60 STAN. L. REV. 1345, 1346 (2008).

⁶³ WENRAN JIANG, CANADIAN INT’L COUNCIL, THE DRAGON RETURNS: CANADA IN CHINA’S QUEST FOR ENERGY SECURITY, CHINA PAPERS NO. 19, at 16 (2010), available at http://www.opencanada.org/wp-content/uploads/2011/05/The-Dragon-Returns_-Canada-in-China%E2%80%99s-Quest-for-Energy-Security-Wenran-Jiang1.pdf.

⁶⁴ *Id.*

⁶⁵ For additional analysis on this point, see generally Larry Catá Backer, *Sovereign Investing in Times of Crisis: Global Regulation of Sovereign Wealth Funds, State-Owned Enterprises and the Chinese Experience*, 19 TRANSNAT’L L. & CONTEMP. PROBS. 3 (2010).

SWFs also serve as a means for countries to protect against fluctuations in revenue as demand and commodities prices change. As commodity prices fluctuate, governments that are dependent on commodity sales for a portion of their revenues may have difficulty in planning expenditures in the face of revenue volatility. As Monk explains, “volatile commodity revenues have a negative impact on the growth of resource-rich countries. Fluctuating revenues make it extremely difficult to pursue a prudent fiscal policy, especially over the long-term which, in turn, aggravates other problems in resource economies.”⁶⁶ Used in this way, SWFs serve as a kind of self-renewing rainy-day fund that may be drawn down to maintain domestic economic stability.

SWFs are also thought to be a mechanism for ensuring intergenerational equity; this is particularly true of SWFs that are based on severance tax revenues. Intergenerational equity may refer to an imperative to save present capital in order to use it to satisfy future commitments, such as pension benefits, or as an imperative to save it specifically for the benefit of future generations, irrespective of commitments to present generations. Intergenerational equity can also refer to a principle of distributive justice: the primary concern in this sense of the term is that future generations should be able to enjoy the fruits of the nation’s resources just as present generations have.⁶⁷ Thus, a SWF is not saving to (or merely to) provide a present generation with an acceptable standard of retirement benefits, but that future generations should also benefit from the sale of a finite store of resources taken from the land that they are to inherit.

Additionally, SWFs can be explained as a tool to preserve autonomy and sovereignty. This function may occur first at the level of the citizenry of the SWF sponsor state or, second, at the level of the elites that govern the SWF sponsor state.⁶⁸

As one considers the uses of state-controlled pension funds—the provision of benefits to citizens and government employees at some future date—and the uses of sovereign wealth funds—as protection against “Dutch Disease”—they may be seen as potential mercantilist policy instrumentalities. SWFs operate in many different ways and may be used as part of broad economic policies (e.g., the SWF being used as a means to insure the supply of industrial inputs, such as rare raw materials), for revenue-smoothing purposes, or to preserve the

⁶⁶ Ashby H. B. Monk, *Sovereignty in the Era of Global Capitalism* 9 (Apr. 10, 2010) (unpublished manuscript) (citations omitted) (citing RICHARD M. AUTY & RAYMOND F. MIKESSELL, *SUSTAINABLE DEVELOPMENT IN MINERAL ECONOMIES* (1998)), available at <http://ssrn.com/abstract=1587327>; see also Paul Stevens, *Resource Impact—Curse or Blessing?*, 9 J. OF ENERGY LITERATURE 3, 13 (2003). See generally Raymond F. Mikesell, *Explaining the Resource Curse, with Special Reference to Mineral-Exporting Countries*, 23 RESOURCES POLICY 191 (1997); Kyle Hatton & Katharina Pistor, *Maximizing Autonomy in the Shadow of Great Powers: The Political Economy of Sovereign Wealth Funds*, 50 COLUM. J. TRANSNAT’L L. 1 (2011).

⁶⁷ Brett M. Frischmann, *Some Thoughts on Shortsightedness and Intergenerational Equity*, 36 LOY. U. CHI. L.J. 457, 459–60 (2005).

⁶⁸ Monk, *supra* note 67, at 23–24.

autonomy of the state-sponsor or its political elites. To be sure, SWFs are often simply used to profitably deploy otherwise inactive funds, but even though such a use is primarily economic rather than political, one could still anticipate the argument that *any* usage by the state is necessarily political, since the state still retains ultimate (if not proximate) control over the assets⁶⁹ and ultimately accepts or distributes the benefits flowing from the investment of the assets. Thus, in these instances, one can plausibly argue that SWFs and public pension funds are used to promote governmental policies, and thus qualify as instrumentalities of foreign governments in the sense that they perform a service on behalf of the government and its citizens. Furthermore, in some cases the fund's officials are explicitly designated as foreign officials by the foreign government. This is the case with China's SWF, the China Investment Corporation (CIC):

CIC is viewed as a full ministerial enterprise. As a well-known practice and part of the command and control economy's legacy, almost all the state or collectively owned enterprises and their leaders are categorized into different administrative levels like civil servants. They have been periodically scaled and estimated by the State Assets Supervision and Administration Commission (SASAC), and the Organization Department of the Communist Party of China (CPC), in terms of administrative ranking, such as full-ministerial, deputy-ministerial, and so on, according to the strategic importance and performance of the enterprises in their charge. And the leaders' promotion and remuneration are, in a large part, determined by the evaluation of these agencies.

....

... It is believed that CIC is a full ministerial-level enterprise, ranking higher than common SOEs under the supervision of the central government [State Assets Supervision and Administration Commission]. This is because [CIC chairman] Lou is the former Vice-Secretary-General of the State Council, a full ministerial-level position, and all the other directors are deputy-ministerial cadres. Therefore, in terms of administrative ranks, CIC is a rare enterprise controlled directly by the State Council and enjoys similar (if not the same) political status as the [People's Bank of China], SASAC, Finance Ministry, or Commercial Ministry.⁷⁰

On the other hand, while state funds may fulfill governmental functions, they also tend to operate relatively autonomously. There are important exceptions—CIC, for example, because of its tighter linkage to the central government and its apparent use as part of the government's "go-out" strategy—but even in these cases the funds are typically used in ways that

⁶⁹ Although not typical, in some cases, such as with the Singaporean Temasek fund, the fund itself is the legal owner of the assets. Li Hong, *Depoliticization and Regulation of Sovereign Wealth Funds: A Chinese Perspective*, 1 ASIAN J. OF INT'L L. 403, 412 (2011). In these cases, it may be easier to distinguish the fund from the central government and make it perhaps less likely that the fund managers would be found to be foreign officials under the FCPA.

⁷⁰ See *id.* at 410–11 (footnotes omitted).

minimize their political effects. There are a number of reasons why a state would insulate its SWF from political influence, and similar justifications also apply to state-controlled pension funds. First and foremost, state fund investments are routinely reviewed and regulated by host nations, especially in cases where the state fund might obtain a controlling interest in the target enterprise. To avoid the possibility of an investment being seen as politically motivated (which may in turn engender a political response from the host state, or at least increase the transaction costs associated with the investment),⁷¹ SWFs often take non-controlling stakes when investing in U.S. enterprises, and also avoid investing in sensitive industries. Furthermore, state funds will often utilize various governance mechanisms to distance the fund investment decision from political interference⁷² and may also insulate investments by giving investment power to outside managers. As a general matter, SWFs are increasingly managed by sophisticated professional staff, not by government bureaucrats. What seems clear is that to the extent that SWFs are linked to governmental policies, influence flows downward from government officials to the fund. Certainly, there are cases in which there is a clear link between the government and the fund as an instrumentality. To take what is probably the most egregious example, the Libyan SWF, the Libyan Arab African Investment Company, was partly used as a means for Moammar Kaddafi to support other autocratic regimes.⁷³

As summarized below, the top-down approach set out in existing tests for whether a state-controlled enterprise or fund is an instrumentality of the foreign government would result in the categorization of many SWFs and pension funds as instrumentalities of the foreign government, and of their employees as foreign officials.

[Tabular material on following page]

⁷¹ See Rose, *supra* note 36, at 1217.

⁷² Li Hong, *supra* note 70, at 411.

⁷³ Jason Mosley, *Post-revolutionary Libyan investment in Africa*, OXFORD SWF PROJECT (Sept. 9, 2011), <http://oxfordswfproject.com/2011/09/09/guest-post-post-revolutionary-libyan-investment-in-africa/>.

Table 1: Aguilar *Factors*

Aguilar <i>Factors</i>	<i>Applicability to State Funds</i>
The entity provides a service to the citizens of the jurisdiction.	<i>Yes</i>
The key officers and directors of the entity are, or are appointed by, government officials.	<i>Yes (appointed)</i>
The entity is financed, at least in large measure, through governmental appropriations or through revenues obtained as a result of government-mandated taxes, licenses, fees, or royalties.	<i>Yes</i>
The entity is vested with and exercises exclusive or controlling power to administer its designated functions.	<i>Yes, typically</i>
The entity is widely perceived and understood to be performing official (<i>i.e.</i> , governmental) functions.	<i>Yes, although the functions are typically economic in nature.</i>

Table 2: Carson *Factors*

Carson <i>Factors</i>	<i>Applicability to State Funds</i>
The foreign state's characterization of the entity and its employees	<i>Often viewed as employees of the fund (and may even be foreign nationals), not as governmental officials (with important exceptions, such as the CIC)</i>
The foreign state's degree of control over the entity	<i>Varies, but many state funds run relatively autonomously (especially with respect to non-economic decisions)</i>
The purpose of the entity's activities	<i>Generally economic in nature, although the purposes vary from fund to fund</i>
The entity's obligations and privileges under the foreign state's law, including whether the entity exercises exclusive or controlling power to administer its designated functions	<i>Yes, typically</i>

Carson Factors	<i>Applicability to State Funds</i>
The circumstances surrounding the entity's creation	<i>Typically they are expressly created to serve particular economic functions.</i>
The foreign state's extent of ownership of the entity, including the level of financial support by the state (e.g., subsidies, special tax treatment, and loans)	<i>The funds are typically (and entirely) drawn from severance taxes or currency reserves.</i>

Yet as noted earlier, even if we characterize many of these funds as instrumentalities under these tests, the basic flaw in the tests is that they fail to link the instrumentality's "foreign officials" with foreign policy. The professional management of many (if not most) SWFs and state-controlled pension funds typically obviates any link with foreign policy. Consider a typical fund manager at a state-owned pension fund. How is he compensated? Often, compensation is based on fund returns, which naturally lead the manager to pursue value-maximizing transactions. What is the consequence of a failure to achieve fund benchmarks? Ultimately, termination. To be sure, a fund manager may take a bribe under the assumption that the transaction at issue will still allow him or her to achieve fund benchmarks, or that the bribe more than offsets the compensation increase he might have received had he selected a more profitable transaction. Because fund managers are typically compensated based on performance, however, there is at least some measure of protection against value-decreasing corruption. Aside from this minor point, however, is the more central question: what is the likelihood that a fund manager would be able to affect foreign policy through his investment decisions? Suppose, for example, that a U.S. asset management firm is competing for the business of a sovereign wealth fund or public pension fund (external asset managers often receive mandates to manage a portion of state fund assets). Does the payment of a bribe by an employee of the firm to a state fund employee implicate foreign policy? Perhaps in the case of the Libyan SWF, ties between U.S. financial firms and Kaddafi's regime did in fact have an effect on U.S. foreign policy. Even in less egregious cases, intelligent and skilled prosecutors could perhaps produce many arguments for the proposition that the payment of any bribe by U.S. asset managers affects foreign policy. Shouldn't we require them to make the arguments?

IV. CONCLUSION

In this Article I argue that two "links" must be secure in order to find a foreign official under the FCPA within the context of state capitalism. The first is the link between the foreign government and the fund. The second is the link

between the instrumentality and the foreign official, which, of course, connects the foreign official back to the FCPA.

In the first instance, it is unclear whether the FCPA should be read to cover sovereign wealth funds and state-controlled pension funds. As I have argued above, many of these funds operate as quasi-independent entities that should not be viewed as direct agents of their respective governments. That being said, there are many cases in which it could reasonably be argued by prosecutors that most state funds serve some government purpose. While many of these funds are designed to serve economic goals, the line between political and economic decisions is often blurred. Is using a sovereign wealth fund to help smooth revenue fluctuations an economic purpose or a political purpose, if the government knows that it must do so in order to have funds available in difficult times to pay for basic public services? This is not to say, of course, that most of these funds invest politically—that a particular investment is politically motivated. Indeed, for the most part, SWFs and state-controlled pension funds are passive, long-term investors.⁷⁴ But I will concede that the reason for which many funds were created, and the purposes they serve, could fairly be characterized as having at least a hybrid political–economic motivation.

Even if we characterize many of these funds as instrumentalities under these tests (which might be the case if one follows the tests set out in *Carson* and *Aguilar*), the basic flaw in the tests is that they fail to link the instrumentality’s “foreign officials” with foreign policy. To see the problems with a unidirectional approach to issues of control, I have attempted to show the effects and the beneficiaries of enforcement of current tests which address one, but not both, of these links. If the test looks only to whether an instrumentality is linked to the government, it does not address the issue of whether a payment has any effect on foreign policy because it does not test whether the bribed foreign official has any impact on foreign policy considerations. It merely looks at whether an employee of the instrumentality is receiving a payment that, in keeping with his or her fiduciary responsibilities, he or she should not accept. To take one of the more egregious examples from 2011, do the purchasing decisions of a liquor store employee of a state-owned liquor store affect foreign policy? In this case it may have been perfectly sensible to conclude that the liquor stores were, in fact, state-owned enterprises, but this shows how such a top-down approach can produce ridiculous results without the limiting principle supplied by a bottom-up analysis of the impact of the alleged foreign official on the instrumentality and the government. Do their decisions impact foreign policy? It is this key consideration that has been missing in most discussions of the foreign-official definition, and should be part of the courts’ analysis if the FCPA is to serve its intended purpose as a tool of foreign policy.

⁷⁴ Paul Rose, *Sovereign Wealth Funds: Active or Passive Investors?*, 118 YALE L.J. POCKET PART 104, 107–08 (2008), <http://thepocketpart.org/2008/11/24/rose.html>.

